No. 91-699

Supreme Court, U.S.
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In The

Supreme Court of the United States

October Term, 1991

JOSEPH J. WALTMAN,

Petitioner,

vs.

FAHNESTOCK & CO., INC.,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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QUESTION PRESENTED

Section 2 of the Federal Arbitration Act, 9 U.S.C. §2, mandates the enforcement of arbitration agreements, and withdraws from the states the power to require a judicial forum for the resolution of claims which the contracting parties agree to resolve by arbitration. *Southland Corp. v. Keating*, 465 U.S. 1 (1984). New York state law prohibits arbitrators from awarding punitive damages, reserving that power to the courts. *Garrity v. Lyle Stuart, Inc.*, 40 N.Y.2d 354, 353 N.E. 2d 793, 386 N.Y.S.2d 831 (1976).

The question therefore presented is:

Whether New York state law, prohibiting the arbitrability of punitive damage awards and thereby directly conflicting with the Federal Arbitration Act, may be applied to vacate an award of punitive damages in a federally regulated industry which compels arbitration of all claims and controversies, merely because the proceeding was challenged in federal court by reason of diversity of citizenship.

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No.

In The

SUPREME COURT OF THE UNITED STATES

October Term, 1991

JOSEPH J. WALTMAN,

Petitioner,

vs.

FAHNESTOCK & CO., INC.,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

To the Honorable the Chief Justice and Associate Justices of the Supreme Court of the United States:

The petitioner, Joseph J. Waltman, respectfully prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Second Circuit, entered in the above-entitled proceeding on June 10, 1991.

OPINIONS BELOW

1. The order of the United States Court of Appeals for the Second Circuit denying rehearing, dated and entered July 26, 1991, is printed in the Appendix hereto, *infra* at p. A-1. It has not been reported.

2. The opinion and judgment of the United States Court of Appeals for the Second Circuit, dated and entered June 10, 1991 is printed in the Appendix hereto, *infra* at p. A-3. It is reported at 935 F.2d 512 (1991).

3. The opinion and order of the District Court, dated August 22, 1990, is printed in the Appendix, hereto, *infra* at p. A-26. It has not been reported.

JURISDICTION

This Petition seeks review of the judgment of the United States Court of Appeals for the Second Circuit entered on June 10, 1991. A timely petition for rehearing was denied on July 26, 1991.

The jurisdiction of this Court to review the judgment of the Second Circuit is invoked under 28 U.S.C. §1254(1).

STATUTORY AND CONSTITUTIONAL PROVISIONS INVOLVED

Article VI, Clause 2 of the Constitution of the United States is reprinted in the Appendix hereto, *infra* at p. A-44.

The federal Arbitration Act, Title 9, U.S.C. § 2 and § 10 are printed in the appendix hereto, *infra* at p. A-44.

STATEMENT OF THE CASE

Procedural History

The genesis of this Petition is an arbitration award in favor of the Petitioner, Joseph Waltman ("Waltman"), arising out of an arbitration proceeding initiated by the Respondent, Fahnestock, a New York brokerage firm. This arbitration proceeding, conducted under the auspices of and pursuant to the Rules of the New York Stock Exchange, began on November 30, 1989, and continued for eight sessions. On January 19, 1990, the arbitrators issued an award in favor of Waltman on his counterclaim of wrongful discharge and defamation against his former employer, Fahnestock. The Award included compensatory damages in the amount of $56,000.00, legal fees in the amount of $14,000.00, damages for defamation in the amount of $100,000.00 and punitive damages in the amount of $100,000.00.

Fahnestock filed a Petition to Vacate the Arbitration Award pursuant to the Federal Arbitration Act, 9 U.S.C. §10, in the United States District Court for the Southern District of New York, invoking the District Court's jurisdiction on the basis of diversity, thereby staying action on Waltman's Petition to Confirm the Award in the United States District Court for the Eastern District of Pennsylvania where Waltman had conducted his insurance business for Fahnestock.

In the Opinion and Order dated August 20, 1990, the District Court denied Fahnestock's Petition to Vacate the damages for defamation but vacated the arbitrators' award of punitive damages. This Order was affirmed by the Second Circuit Court of Appeals on June 10, 1991. (Judge Mahoney dissenting on the issue of punitive damages.) Waltman filed a Petition for Rehearing which was denied on July 26, 1991.

STATEMENT OF FACTS

Joseph Waltman was hired by Fahnestock on March 15, 1982, to establish and oversee a Retirement Trust Division which would service Fahnestock's custodial retirement accounts. Waltman was terminated from his employment without notice or severance pay on December 12, 1988, two weeks before Christmas and told to leave the office immediately. The reason given for the termination was Fahnestock's alleged lack of interest in marketing insurance products, the business which Waltman developed for Fahnestock in 1985 through the establishment of a General Agency to market products for Keystone Provident Life Insurance Company, and which operated out of his office in Bala Cynwyd, Pennsylvania.

Waltman had also initiated Fahnestock's corporate licensing for insurance purposes in New York State, a process which began in June, 1987, after Waltman personally complied with New York State's individual licensing requirements in order to act as Fahnestock's insurance sub-licensee. As a further part of this licensing process, Fahnestock retained Pershing Insurance Services ("Pershing") to represent it during the licensing process and to maintain the documentation concerning agent licensing.

Shortly after Fahnestock was acquired by Edward A. Viner Holdings Ltd. in 1988, Waltman was told to relinquish his position as the sub-licensee of the corporation and to turn over all the New York State corporate licensing forms to E. Stephen Walsh. Waltman complied with these instructions and turned over the corporate licensing forms on December 8, 1988, two weeks prior to his abrupt dismissal from employment. Subsequent to his termination and after waiting three weeks to hear from Fahnestock concerning the issue of severance pay, Waltman was asked by Walsh to assist Walsh in completing the corporate licensing forms for the New York State Insurance Department and to address questions by Fahnestock's registered representatives concerning their licenses.

Waltman telephoned Walsh on January 18, 1989, to suggest that the issue of severance pay be resolved first. As Waltman set forth in his Counterclaim, the conversation with Walsh resolved nothing and Walsh told Waltman to provide him with whatever information he had concerning the registered agents and he would proceed without Waltman's assistance. Waltman stated that the files he maintained were the property of his general agency and would not be of use to Walsh. Fahnestock's response, in a telephone message delivered by Walsh on January 19, 1990, was to threaten Waltman with immediate arrest if he did not return the files by that Friday. On the advice of counsel, Waltman wrote to Fahnestock, provided a list of agents appointed through his agency and requested a written release from each agent prior to the release of any information from his files.

Instead of complying with Waltman's request, Fahnestock filed a Statement of Claim with the New York Stock Exchange accusing him of taking files from the firm

and further alleging that the files at issue were maintained at Fahnestock's request and direction. Waltman filed an answer in the N.Y.S.E. arbitration and a counterclaim. Fahnestock also filed an amended U-5 form with the New York Stock Exchange which stated that Waltman was terminated as a result of "business consolidation", but was also "under internal review for fraud or wrongful taking of property or violating investment-related statutes . . ." The falsity of Fahnestock's charges was established during the arbitration proceedings.

During the course of eight hearings, the arbitrators heard testimony proving that the personnel files in question were readily available to Fahnestock because they were maintained by Pershing, that certain files were already in Fahnestock's possession, and that Waltman maintained only copies of documentation provided by Keystone Insurance Company concerning each registered representative. Waltman proved that Fahnestock's chairman threatened him with arrest and further established that the chairman instructed that the amended U-5 form was to be filed "in such a way as to indicate that [Waltman] had been fired for cause and noting that he had stolen property from Fahnestock," through the testimony of Edward F. O'Rourke, Fahnestock's former Managing Director. O'Rourke also testified that a blemished U-5 form would probably eliminate Waltman as a candidate for a job. Gene R. Samit, President of a subsidiary for Wilmington Trust, WDC Capital Chargers, testified that in a discussion with Waltman regarding a job, once the question of a blemished U-5 form was mentioned, Mr. Waltman was removed from consideration. Fahnestock also tried to get Waltman to drop his counterclaim by putting pressure on his new employer, SFT Fund Group, which had a substantial business relationship with Fahnestock.

This substantive, unrebutted testimony, which represents only a small portion of a 750 page hearing transcript, convinced three arbitrators that Fahnestock's course of conduct toward Waltman warranted not only compensatory damages for wrongful discharge and defamation but substantial punitive damages. The Award of Arbitrators was not based solely on the filing of the Amended Form U-5 but on Fahnestock's entire course of conduct in attempting to damage Waltman's career and reputation and pressure him to drop his counterclaim.

The plurality decision of the Second Circuit, while affirming the compensatory and defamation damages, held that the arbitrators exceeded their power by awarding punitive damages to Waltman, applying New York state law to the propriety of a punitive damage award by arbitrators because the award was before the District Court on the basis of diversity of citizenship. The dissenting opinion concluded that "state law which limits freedom of contract with respect to arbitration agreement covered by the [Federal Arbitration Act ("FAA")] conflicts with the FAA and is preempted by it." (Appendix, p. A-21). The Second Circuit's decision in this case conflicts with the decisions of two Circuit Courts of Appeals and, your petitioner believes, incorrectly applies state law to arbitration proceedings conducted under the auspices of a federally regulated industry which requires by its rules compulsory arbitration of all claims and controversies. (Appendix, p. A-46). In so doing, the Second Circuit's decision undermines this Court's consistent adherence to a federal policy which favors arbitration and disrupts the uniform application of federal substantive law to securities industry arbitration proceedings.

REASONS FOR GRANTING THE WRIT

I. THIS COURT SHOULD GRANT CERTIORARI TO RESOLVE THE CONFLICT AMONG THE CIRCUITS AS TO WHETHER ARBITRATORS IN A PROCEEDING SUBJECT TO THE FEDERAL ARBITRATION ACT HAVE THE POWER AND AUTHORITY TO AWARD PUNITIVE DAMAGES

PRELIMINARY STATEMENT

The Second Circuit's decision that state law determines whether arbitrators may award punitive damages is contrary to the decisions of every federal court which has confronted the issue of arbitrability of punitive damages. The decision also frustrates the clearly articulated policies of this Court to broadly construe arbitration agreements. The Second Circuit's decision imposes a severe limitation on the arbitrability of issues arising out of disputes in the securities industry which are governed by the Rules of the New York Stock Exchange. Since these disputes are arbitrated throughout the United States and relate to commerce, they are subject to the Federal Arbitration Act, 9 U.S.C. § 1 *et seq.* Although the Rules of the New York Stock Exchange are silent on the issue of whether arbitrators may award punitive damages, the award forms expressly provide space for the award of punitive damages. Because these arbitration proceedings take place throughout the United States and, in some instances (although not in this one) may be subject to varying choice-of-law provisions, some of which would conflict with the Rules of the New York Stock Exchange, this Court's decision is necessary to ensure the uniform treatment of parties in this federally regulated industry.

A. THE SECOND CIRCUIT DECISION CONFLICTS WITH THE FIRST AND ELEVENTH CIRCUIT DECISIONS WHICH REST ON FEDERAL POLICIES FAVORING ARBITRATION OF ALL CLAIMS NOT EXPRESSLY EXCLUDED BY CONTRACT

The Second Circuit decision relied on *Garrity v. Lyle Stuart, Inc.*, 40 N.Y.2d 354, 353 N.E. 2d 793, 386 N.Y.S.2d 831 (1976), a case which has been rejected and severely criticized by every Circuit Court of Appeals and District Court which has considered it, even where the pertinent contract expressly stated that it was to be governed by New York Law. *Raytheon Co. v. Automated Business Systems, Inc.*, 882 F.2d 6 (1st Cir. 1989); *Bonar v. Dean Witter Reynolds, Inc.*, 835 F.2d 1378 (11th Cir. 1988); *Willoughby Roofing & Supply Co., Inc. v. Kajima International, Inc.*, 598 F.Supp. 353 (N.D. Ala. 1984), *aff'd.*, 776 F.2d 269 (11th Cir. 1985) (per curiam); *Pyle v. Securities U.S.A., Inc.*, 758 F.Supp. 638 (D. Colo. 1991); *Barbier v. Shearson Lehman Hutton*, 752 F.Supp. 151 (S.D.N.Y. 1990), appeal pending; *Singer v. E.F. Hutton & Co.*, 699 F.Supp. 276 (S.D. Fla. 1988); *Willis v. Shearson/American Express, Inc.*, 569 F.Supp. 821 (M.D. N.C. 1983); *Ehrich v. A.G. Edwards & Sons, Inc.*, 675 F.Supp. 559 (D.S.D. 1987).

In *Raytheon Co. v. Automated Business Systems, Inc., supra*, the First Circuit was faced with a contract which did not specifically provide for the award of punitive damages and contained a choice of law provision. The First Circuit held that its analysis was governed by the broad policies of the Federal Arbitration Act recognizing this Court's policy that:

> "any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration, whether the problem at hand is the construction of the contract itself or an allegation of waiver, delay, or a like defense to arbitrability." *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*, 460 U.S. 1, 24-25 (1983).

The First Circuit rigorously analyzed the arbitration clause at issue. Noting that the arbitration clause at issue was not limited in scope or application, the First Circuit held that in the context of a commercial arbitration to which the Federal Arbitration Act applied, punitive damages may be awarded as an effective deterrent to malicious or fraudulent conduct:

> Where such conduct could give rise to punitive damages if proved to a court, there is no compelling reason to prohibit a party which proves the same conduct to a panel of arbitrators from recovering the same damages. Certainly, the fact that the parties agreed to resolve their dispute through an expedited and less formal procedure does not mean that they should be required to surrender a legitimate claim to damages. Parties that do wish arbitration provisions to exclude punitive damages claims are free to draft agreements that do so explicitly. *Raytheon Co., supra.* at p. 12.

The First Circuit's decision thus directly conflicts with the Second Circuit's decision which not only embraced the *Garrity* rule prohibiting arbitrators from awarding punitive damages but implied a limitation to the arbitration rules at issue.

Similarly, in *Bonar v. Dean Witter Reynolds, Inc., supra.*, the Eleventh Circuit specifically rejected *Garrity* on the ground that the customer agreement at issue was governed by the Federal Arbitration Act, even where the contract provided that New York law applied, stating that "a choice of law provision in a contract merely designates the substantive law that the arbitrators must apply in determining whether the conduct of the parties warrants an award of punitive damages; it does not deprive the arbitrators of their authority to award punitive damages." *Id.* at 1387, citing *Willoughby, supra.* at 598 F.Supp. 359. The Eleventh Circuit adopted a rule permitting the arbitrability of punitive damage claims in reliance on this Court's holding in *Moses H. Cone Memorial Hospital, supra.* at 24-25, squarely rejecting the application of state law to determine whether arbitrators have authority to award punitive damages in favor of federal policy which requires the Court to effectuate the intent of the parties.

B. NEW YORK STATE LAW LIMITING FREEDOM OF CONTRACT CONFLICTS WITH THE FEDERAL ARBITRATION ACT AND IS PREEMPTED BY IT

In this case, arising out of an employment dispute, petitioner Waltman's employment with Fahnestock was conditioned on his agreement to submit to arbitration under the auspices of the New York Stock Exchange. The Rules of the New York Stock Exchange, including Rule 347 governing employment disputes, are exceedingly broad and do not contain any choice-of-law provision. There is no limitation on the kinds of controversies to be submitted or the damages to be awarded. (Appendix, p. A-46) However,

because the Rules do not expressly state that arbitrators may award punitive damages, the Second Circuit implied an exclusion. (Appendix, p. A-15) This implied exclusion is contrary to basic federal policy which mandates resolving any doubt concerning arbitrability in favor of arbitration. *Moses H. Cone Memorial Hospital, supra; Willoughby Roofing & Supply Co., Inc., supra.*

The Second Circuit's reliance on *Garrity* as controlling as a matter of law directly conflicts with the First and Eleventh Circuits with regard to the applicability of state law to contracts within the purview of the Federal Arbitration Act and the power of arbitrators to award punitive damages where the parties' agreement does not expressly exclude them. This conflict can only be resolved by this Court and should be resolved to prevent continued conflict, confusion, potential forum shopping and disparate results.

As the Second Circuit recognized, the *Garrity* rule "is bottomed on state policy considerations deemed controlling by New York's highest court" (Appendix, p. A-13) that punitive damages are a form of sanction reserved for the State. *Garrity* has been sharply criticized as "an anomaly, frustrating the goals of fairness and finality that are the essence of arbitration and undermining the valuable role that punitive damages play in deterring fraudulent or malicious conduct." Stipanowich, "Punitive Damages in Arbitration: Garrity v. Lyle Stuart, Inc. Reconsidered," 66 Boston L.Rev. 953 (1966). Further, the *Garrity* rule, conflicts with this Court's opinion in *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 238-242 (1987) that punitive damages may be arbitrated, at least in the context of RICO claims, suggesting that New York public policy concerns about sanctions reserved to the state conflict with

strong federal policy considerations governing the breadth and scope of arbitration agreements. As this Court stated in *Volt Information Sciences, Inc. v. Board of Trustees,* 489 U.S. 468, 477 (1989):

> . . . even when Congress has not completely displaced state regulation in an area, state law may nonetheless be preempted to the extent that it actually conflicts with federal law--that is, to the extent that it "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." *Hines v. Davidowitz,* 312 U.S. 52, 67 (1941).

C. THE SECOND CIRCUIT'S DECISION ERRONEOUSLY APPLIED STATE LAW TO DETERMINE WHETHER ARBITRATORS HAVE THE POWER TO AWARD PUNITIVE DAMAGES

In its decision, the Second Circuit disregarded and ignored the concept of federal substantive law articulated by this Court in *Moses H. Cone Memorial Hospital v. Mercury Construction Corp., supra.* and, relying solely on its diversity jurisdiction, held that New York state law, which prohibits arbitrators from awarding punitive damages as a matter of state public policy, provides the rule of decision for arbitrations conducted in New York State (Appendix, p. A-15). Your petitioner respectfully submits that the majority opinion inappropriately applied the rule enunciated by this Court in *Erie v. Tompkins,* 304 U.S. 64 (1938) to a matter in which federal law should supply the rule of

decision, as Judge Mahoney stated in his dissent (Appendix, p. A-20).

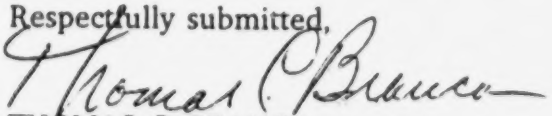
This Court has previously rejected attempts to impose state law on arbitration proceedings which are challenged in federal court solely by reason of diversity of citizenship. *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395 (1967). Likewise, numerous Circuit Courts of Appeals have recognized the preemptive effect of the Federal Arbitration Act in the light of limiting and inconsistent state law. *Foster v. Turley*, 808 F.2d 38 (10th Cir. 1986); *Saturn Distribution Corp. v. Williams*, 905 F.2d 719 (4th Cir. 1990), *cert. denied*, 111 S. Ct. 516 (1990); *Osterneck v. Merrill, Lynch, Pierce, Fenner & Smith*, 841 F.2d 508 (3d Cir. 1988); *Securities Industry Association v. Connolly*, 883 F.2d 1114 (1st Cir. 1989); *Sanders-Midwest v. Midwest Pipe Fabricators, Inc.*, 857 F.2d 1235 (8th Cir. 1988).

The Second Circuit's failure and refusal to adhere to the principle enunciated by this Court and every Circuit which has decided the issue, that traditional choice of law principles in diversity actions are not available when the Federal Arbitration Act applies, warrants this Court's review because the decision is contrary to the intent of Congress in passing the Federal Arbitration Act to "simply require[s] courts to enforce privately negotiated agreements to arbitrate, like other contracts, in accordance with their terms." *Volt Information Sciences, Inc. v. Board of Trustees, supra.*, and to resolve any doubt in favor of arbitration. *Moses H. Cone Memorial Hospital, supra.*

CONCLUSION

The Second Circuit's application of state law to the issue of whether arbitrators have the power to award punitive damages is a blatant departure from this Court's policies concerning the liberal construction of arbitration clauses and stands alone as an egregious attempt to limit the scope of arbitration proceedings. The conflict thus created by the Second Circuit's decision has far-reaching consequences for parties subject to compulsory arbitration in the securities industry and otherwise since, absent this Court's review, judicial review of federal arbitration awards will lack uniformity. The issue presented to this Court is ripe for review because of the conflict between the Circuits and because the Second Circuit's decision conflicts with the intent of Congress in passing the Federal Arbitration Act and the policies articulated by this Court.

Respectfully submitted,



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UNITED STATES COURT OF APPEALS

FOR THE

SECOND CIRCUIT

At a stated term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse, in the City of New York, on the twenty-sixth day of July, one thousand nine hundred and ninety one.

FAHNESTOCK & CO., INC.,
Petitioner-Appellant
Cross-Appellee,

-v-

JOSEPH J. WALTMAN,
Respondent-Appellee
Cross-Appellant.

DOCKET NUMBER

90-7867
90-7869

A petition for rehearing containing a suggestiont hat the action be reheard in banc having been filed herein by Respondent-Appellee, Cross-Appellant, Joseph J. Waltman.

Upon consideration by the panel that hard the appeal, it is

Ordered that said petition for rehearing is DENIED.

It is further noted that the suggestion for rehearing in banc has been transmitted to the judges of the court in regular active service and to any other judge that heard the appeal and that no such judge has requested that a vote be taken thereon.

ELAINE B. GOLDSMITH
Clerk

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

Nos. 927, 928-August Term, 1990
(Argued: January 24, 1991 Decided: June 10, 1991)
Docket Nos. 90-7867, -7869

In the Matter of the New York Stock Exchange
Arbitration between,
FAHNESTOCK & CO., INC.,
Petitioner-Appellant,
Cross-Appellee,

-against-

JOSEPH J. WALTMAN,
Respondent-Appellee,
Cross-Appellant.

Before:
VAN GRAAFEILAND, NUNER and MAHONEY,
Circuit Judges.

Appeal and cross-appeal from judgment entered in United States District Court for the Southern District of New York (Leisure, J.) confirming compensatory damages

portion, and vacating punitive damages portion, of arbitration award against stock brokerage firm for defamation of discharged employee.

Judgment affirmed in all respects.

Judge Mahoney concurs in part and dissents in part in a separate opinion.

LEE D. UNTERMAN, New York, NY (Patricia L. Moore, Broudy & Jacobson, New York, NY, of counsel), for Petitioner-Appellant, Cross-Appellee.

ROBERT SCANDONE, Philadelphia, PA (Mark J. Astarita, Gusrae, Kaplan & Bruno, New York, NY, Jane R. Goldberg, of counsel), for Respondent-Appellee, Cross-Appellant.

Paul Windels III, New York, NY (Perry & Windels, New York, NY, William J. Fitzpatrick, Gerard J. Quinn, New York, NY, of counsel), submitted a brief for amicus curias the Securities Industry Association, Inc.

MINER, Circuit Judge:

Petitioner-appellant, Fahnestock & Co., Inc. ("Fahnestock") appeals from a judgment entered in the United States District Court for the Southern District of New York (Leisure, J.) confirming the compensatory damages portion of an arbitration award in favor of its former employee, Joseph J. Waltman. Waltman cross-appeals from the same judgment insofar as it vacates the punitive damages portion of the arbitration award.

On appeal, Fahnestock contends that the district court erred by denying its petition to vacate the entire defamation award because the members of the arbitration panel ("Arbitrators") exceeded their authority and manifestly disregarded the applicable law. Fahnestock argues that its filing of an amended Form U-5, a termination notice form that the National Association of Securities Dealers ("NASD") requires stock brokerage firms to file when they dismiss an employee, was absolutely privileged and could not serve as a basis for an award for defamation. On cross-appeal, Waltman argues that the court erred in vacating the Arbitrators' award for punitive damages because federal substantive law, as opposed to the New York law applied by the district court, permits such an award in arbitration proceedings brought pursuant to the Federal Arbitration Act ("FAA"), 9 U.S.C. §§ 1-14 (1988). For the reasons that follow, we affirm the judgment of the district court.

BACKGROUND

The arbitration proceeding subject of this action arose as a result of the events surrounding the discharge of Waltman from the employ of Fahnestock. Waltman was hired on March 16, 1982 as a "registered representative to head Fahnestock's Retirement Trust Division" and "to manage and build Fahnestock's insurance products business." During the course of his employment, in addition to overseeing Fahnestock's Retirement Division, Waltman acted as an insurance sub-licensee for Fahnestock. In addition, he established a general insurance agency in Pennsylvania for the purpose of marketing insurance and annuity products for Fahnestock in Pennsylvania and other states. Waltman was discharged on December 12, 1988 when Fahnestock closed down its Retirement Trust Division.

When Waltman was terminated, Fahnestock filed a Form U-5 termination notice with the NASD, indicating that the discharge was occasioned by "business consolidation." When Fahnestock later was unable to locate some insurance files that it believed were maintained by Waltman, it contacted Waltman and requested that he return the files. Waltman refused to return the files, claiming that they belonged to his general insurance agency. Waltman explained that he would turn over the files only if Fahnestock obtained a release and indemnification from each registered agent named in the files.

Instead of complying with Waltman's request, Fahnestock filed a Statement of Claim with the Director of Arbitration of the New York Stock Exchange ("NYSE"), requesting the following relief: return of the original files,

damages and costs, and other expenses. Fahnestock then filed an amended Form U-5. On the amended form, Fahnestock changed its previous answer in response to the question about whether the employee was under "internal review for fraud or wrongful taking of property, for violating investment-related statutes, regulations, rules or industry standards of conduct," from a "NO" to a "YES."

Waltman filed an answer in the NYSE arbitration, denying the allegations that he wrongfully took Fahnestock's property. He also filed a counterclaim, in which he alleged that Fahnestock and three of its officers, the chairman of the board, the president, and the general counsel, defamed him by filing the amended Form U-5.

During the course of eight hearings, the Arbitrators heard testimony concerning the chairman's threats to arrest Waltman for his failure to return the files, the chairman's instruction to refile the Form U-5 "in such a way as to indicate that [Waltman] had been fired for cause and noting that he had stolen property from Fahnestock," and the threats made to Waltman's current employer in an attempt to pressure Waltman into abandoning his defamation action. The Arbitrators awarded Waltman $56,000 in compensatory damages for wrongful discharge, $14,700 in legal fees, $100,000 for defamation and $100,000 in punitive damages. Liability was imposed on Fahnestock alone, and the claims against the individual officers were dismissed.

Waltman filed a petition to confirm the arbitral award under NYSE Arbitration rule 628(a) in the Eastern District of Pennsylvania. On March 15, 1990, Fahnestock filed a petition in the Southern District of New York to vacate the arbitral award under the Federal Arbitration

Act, 9 U.S.C. § 10(d), claiming that the Arbitrators exceeded their authority by granting an award for defamation and by awarding punitive damages. No other challenges to the award were made. Federal jurisdiction was based on the diversity of the parties, as Fahnestock's principal place of business was New York and Waltman resided in Pennsylvania. The Eastern District of Pennsylvania court stayed the petition to confirm the arbitral award pending the outcome of the New York action to vacate it.

On August 22, 1990, the district court denied Fahnestock's petition to vacate the compensatory damages portion of the arbitral award for defamation, but granted its petition to vacate the punitive damages portion of the award. The court rejected Fahnestock's claim that statements made in the amended Form U-5 were absolutely privileged. Instead, it found only a qualified privilege, which could be overcome upon a showing of malice or lack of probable cause for the statement. Holding that a finding of malice or probable cause was a factual matter and, as such, could be reviewed by the courts only on a limited basis, the court found that the Arbitrators did not exceed their powers in rendering the compensatory defamation award.

With respect to the punitive damages portion of the arbitral award, the district court, relying on Garrity v. Lyle Stuart, Inc., 40 N.Y.2d 354, 353 N.E.2d 793, 386 N.Y.S.2d 831 (1976), held that the Arbitrators were prohibited from awarding punitive damages. In response to Fahnestock's contention that federal substantive law governs arbitrations conducted pursuant to the Federal Arbitration Act, the court held that "the state substantive law as set forth in Garrity v. Lyle Stuart, Inc. regarding

the inability of arbitrators to award punitive damages, is not in direct conflict with any express provision of the Federal Arbitration Act," and therefore the application of Garrity would not violate the supremacy clause of the United States Constitution.

DISCUSSION

1. Compensatory Award

An arbitration award may be vacated "[w]here the arbitrators exceeded their powers," 9 U.S.C. § 10(d), or where the arbitrators acted in "manifest disregard of the law." Carte Blanche (Singapore) Pte., Ltd. v. Carte Blanche Int'l, Ltd., 888 F.2d 260, 265 (2d Cir. 1989); Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Bobker, 808 F.2d 930, 933-34 (2d Cir. 1986); Siegel v. Titan Indus. Corp., 779 F.2d 891, 892 (2d Cir. 1985) (per curiam). Fahnestock asserts that the Arbitrators exceeded their powers and manifestly disregarded the law in granting an award for defamation based on its filing of the amended Form U-5. Fahnestock argues that, because it was required by law to file the form, the filing was subject to an absolute privilege. Therefore, it urges that the filing of the Form U-5 could not serve as a basis for an award for defamation. Fahnestock's arguments are without merit.

We have consistently accorded the narrowest reading to section 10(d), "especially when it 'has been invoked in the context of the arbitrators' alleged failure to correctly decide a question which all concede to have been properly submitted in the first instance. Synergy Gas Co. v. Sasso, 853 F.2d 59, 63 (2d Cir.) (citation omitted), cert. denied, 488 U.S. 994 (1988). Consequently, we have

recognized that if arbitrators "rule[] on issues not presented to [them] by the parties, [they have] exceeded [their] authority and the award must be vacated." Dighello v. Busconi, 673 F. Supp. 85, 87 (D. Conn. 1987), aff'd mem., 849 F.2d 1467 (2d Cir. 1988); see Andros Compania Maritima, S.A. v. Marc Rich & Co., A.G., 579 F.2d 691, 703 (2d Cir. 1978). Here, it is uncontested that the ruling of the Arbitrators was confined to the issues presented by the parties. Moreover, we have recognized that defamation claims based on statements in a Form U-5 are arbitrable. See Fleck v. E.F. Hutton Group, Inc., 891 F.2d 1047, 1049, 1053 (2d Cir. 1989). Therefore, any argument that it is beyond the power of arbitrators to decide these types of claims is contrary to the law of this circuit.

Nor are we persuaded that the Arbitrators manifestly disregarded the law in awarding Waltman damages for defamation. Judicial inquiry under the manifest disregard standard likewise is extremely limited. Bobker, 808 F.2d at 933-34. We have held that there must be " 'something beyond and different from a mere error in the law or failure on the part of the arbitrators to understand or apply the law,' " Siegel, 779 F.2d at 892 (citation omitted), in order to sustain a finding of manifest disregard of the law. Illustrative of the degree of "disregard" necessary to support vacatur under this standard is our holding that manifest disregard will be found where an "arbitrator 'understood and correctly stated the law but proceeded to ignore it.' " Id. at 893 (citation omitted).

Under New York law, "[a] communication is said to be qualifiedly privileged where it 'is fairly made by a person in the discharge of some public or private duty, legal or moral, or in the conduct of his own affairs, in a matter

where his interest is concerned." Toker v. Pollak, 44 N.Y.2d 211, 219, 376 N.E.2d 163, 166, 405 N.Y.S.2d 1, 5 (1978); see also Mihlovan v. Grozavu, 72 N.Y.2d 506, 509, 531 N.E.2d 288, 289, 534 N.Y.S.2d 656, 657 (1988) (per curiam); Shapiro v. Health Ins. Plan of Greater New York, 7 N.Y.2d 56, 60, 163 N.E.2d 333, 336, 194 N.Y.S.2d 509, 512-13 (1959). The qualified privilege, however, can be vitiated upon a showing that the communication was made with actual malice. Park Knoll Assocs. v. Schmidt, 59 N.Y.2d 205, 211, 451 N.E.2d 182, 185, 464 N.Y.S.2d 424, 427 (1983); see also Mihlovan, 72 N.Y.2d at 509, 531 N.E.2d at 289, 534 N.Y.S.2d at 657-58. Actual malice has been defined as " 'Personal spite or ill will, or culpable recklessness or negligence.' " Garson v. Hendlin, 141 A.D.2d 55, 64, 532 N.Y.S.2d 776, 782 (2d Depot 1988) (citation omitted).

At the arbitration hearings, the Arbitrators heard testimony that the chairman of Fahnestock, gave instructions to refile the Form U-5 "in such a way as to indicate that [Waltman] had been fired for cause and ... that he had stolen property from Fahnestock." Fahnestock's former managing director testified that the amended Form U-5 was filed at the command of Fahnestock's chairman for the specific purpose of damaging Waltman's reputation rather than for a regulatory purpose. Additionally, evidence was introduced that Fahnestock attempted to force Waltman to drop his counterclaim by threatening his current employer.

Here, the Arbitrators never indicated the reasons for the defamation award. However, it is axiomatic that arbitrators need not disclose the rationale for their award. United Steelworkers of Am. v. Enterprise Wheel & Car Corp., 363 U.S. 593, 598 (1960); Koch Oil, S.A. v.

Transocean Gulf Oil Co., 751 F.2d 551, 554 (2d Cir. 1985). "[If a ground for the arbitrator's decision can be inferred from the facts of the case, the award should be confirmed." Sobel v. Hertz, Warner & Co., 469 F.2d 1211, 1216 (2d Cir. 1972); see Siegel, 779 F.2d at 894. Therefore, even though Fahnestock was protected by the qualified privilege in filing the amended form, based on the evidence, the arbitrators acted well within the bounds of their broad authority in making an award of compensatory damages in favor of Waltman. See In re Marine Pollution Serv., Inc., 857 F.2d 91, 94 (2d Cir. 1988) (any "colorable justification" will support an arbitral award); Andros Compania, 579 F.2d at 704. The ample evidence of Fahnestock's flagrantly spiteful conduct, demonstrating its intent simply to injure Waltman's reputation, presented the Arbitrators with sufficient grounds to find that no qualified privilege attached to Fahnestock's filing of the amended form. See Garson, 141 A.D.2d at 65, 532 N.Y.S.2d at 782. It is apparent that the Arbitrators declined to extend the doctrine of absolute immunity to statements made to the NASD, a quasi-official body. Cf. Toker, 44 N.Y.2d at 222-23, 376 N.E.2d at 168-69, 405 N.Y.S.2d at 7; Garson, 141 A.D.2d at 59-60, 532 N.Y.S.2d at 779. Therefore, under these circumstances, we agree with the district court that the Arbitrators' compensatory defamation award in favor of Waltman should be confirmed.

II. Punitive Damages Award

On cross-appeal, Waltman argues that the district court erred in vacating the punitive damages portion of the Arbitrators' award. The district court perceived that the governing rule was established by the New York Court of

Appeals: "An arbitrator has no power to award punitive damages, even if agreed upon by the parties." Garrity, 40 N.Y.2d at 356, 353 N.E.2d at 795, 386 N.Y.S.2d at 832. The Garrity rule is bottomed on policy considerations deemed controlling by New York's highest court: "[E]nforcement of an [arbitrator's] award of punitive damages as a purely private remedy would violate strong public policy." Id. The rule maintains its vitality in the courts of New York. See, e.g., Diker v. Cathray Constr. Corp., 158 A.D.2d 657, 658, 552 N.Y.S.2d 37, 38 (2d Depot 1990); Belco Petroleum Corp. v. AIG Oil Rig, Inc., 164 A.D.2d 583, ___, 565 N.Y.S.2d 776, 784 (1st Dep't 1991).

Waltman's challenge to the district court judgment is premised on the federal substantive law of arbitrability: "Section 2 [of the FAA, 9 U.S.C. § 2,] is a congressional declaration of a liberal federal policy favoring arbitration agreements .... The effect of the section is to create a body of federal substantive law of arbitrability, applicable to any arbitration agreement within the coverage of the Act." Moses H. Cone Memorial Hosp. v. Mercury Constr. Corp., 460 U.S. 1, 24 (1983). Since the agreement between the parties falls within the coverage of the FAA, allows for the arbitration of any dispute between them and includes no restriction on the award of punitive damages under the governing rules of the New York Stock Exchange, Waltman urges that there should be no bar to the award of punitive damages under federal substantive arbitration law. Indeed, there is precedent for Waltman's position that federal law and policy confers upon FAA arbitrators the right to award punitive damages even where, as is not the case here, the arbitration parties agree that New York law is to govern. See, e.g., Bonar v. Dean Witter Reynolds, Inc., 835 F.2d 1378, 1386-88

(11th Cir. 1988); Barbier v. Shearson Lehman Hutton, Inc., 752 F. Supp. 151 (S.D.N.Y. 1990); Singer v. E.F. Hutton & Co., 699 F. Supp. 276 (S.D. Fla. 1988); Duggal Int'l Inc. v. Sallmetal, B.V., No. 84 Civ. 7170 (JMC) (S.D.N.Y. May 8, 1986). Our view is somewhat different.

While it is true that in enacting the FAA, "Congress intended to foreclose state legislative attempts to undercut the enforceability of arbitration agreements," Southland Corp. v. Keating, 465 U.S. 1, 16 (1984), it also is true that "[t]he FAA contains no express preemptive provision, nor does it reflect a congressional intent to occupy the entire field of arbitration," Volt Info. Sciences v. Board of Trustees of the Leland Stanford Jr. Univ., 489 U.S. 468, 477 (1989). Accordingly, state law may be applied in arbitration matters, subject to preemption only "to the extent that it actually conflicts with federal law." Id.; see also Hines v. Davidowitz, 312 U.S. 52, 67 (1941) (preemption is found in cases where state law "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress."). We find no conflict between the provisions of the FAA and the Garrity rule.

What the FAA requires is that parties comply with their agreements to arbitrate. " '[A]rbitration is a matter of contract and a party cannot be required to submit to arbitration any dispute which he has not agreed so to submit.' " AT&T Technologies, Inc. v. Communications Workers of Am., 475 U.S. 643, 648 (1986) (citation omitted); see also New York News Inc. v. Newspaper Guild of New York, 927 F.2d 82, 84 (2d Cir. 1991); Neechi v. Neechi Sewing Mach. Sales Corp., 348 F.2d 693, 696 (2d Cir. 1965), cert. denied, 383 U.S. 909 (1966). Waltman's defamation claim certainly was a matter for arbitration

pursuant to the agreement of the parties, but there was no agreement as to whether punitive damages were allowable. If the parties had agreed to permit the arbitrators to make such an award, federal arbitration law might require confirmation, for "parties are generally free to structure their arbitration agreements as they see fit," and the FAA provides for enforcement of the terms of such privately negotiated agreements. Volt Information Sciences, 489 U.S. at 478-79. The body of preemptive federal substantive law that supports the FAA has developed largely in response to state laws that restrict arbitration in derogation of agreements freely negotiated. See, e.g., Perry v. Thomas, 482 U.S. 483, 489-90 (1987). The FAA itself was designed "to make arbitration agreements as enforceable as other contracts," Prima Paint Corp. v. Flood & Conklin Mfg. Co., 388 U.S. 395, 404 n. 12 (1967) and "to overrule the judiciary's longstanding refusal to enforce agreements to arbitrate," Dean Witter Reynolds Inc. v. Byrd, 470 U.S. 213, 219-20 (1985). The federal substantive law of arbitration assures the accomplishment of these purposes.

Why should state law be applied in this case, where the parties have not specified remedies and where the arbitrators therefore should be free to fashion appropriate relief? The answer lies in the jurisdictional basis of the action giving rise to this appeal. While the FAA "creates a body of federal substantive law establishing and regulating the duty to honor an agreement to arbitrate, . . . it does not create any independent federal question jurisdiction . . . ." Moses H. Cone, 460 U.S. at 25 n.32. Some independent basis for federal jurisdiction must be established. The petition in the case at bar has invoked the diversity of citizenship of the parties as a means of acquiring subject matter jurisdiction. 28 U.S.C. §§ 1332.

The award of the arbitrators was before the district court in this diversity case for review under state law. As previously noted, state law relating to the propriety of a punitive damages award by arbitrators in the absence of an agreement on the subject is not preempted by any federal substantive law bearing on the subject.

Ordinarily, "[i]n a diversity action, or in any other lawsuit where state law provides the basis of decision, the propriety of an award of punitive damages for the conduct in question ... [is a] question[ ] of state law." Browning-Ferris Indus. v. Kelco Disposal, Inc., 492 U.S. 257, 278 (1989). The measure of damages in general is a matter controlled by New York substantive law where federal jurisdiction in New York is predicated on the diversity of the parties. See Shu-Tao Lin v. McDonnell Douglas Corp., 742 F.2d 45, 49 n.5. (2d Cir. 1984); Van Gemert v. Boeing Co., 553 F.2d 812, 813 (2d Cir. 1977). It follows that in this action the Garrity rule prohibiting the award of punitive damages by arbitration must be applied. That the rule is grounded in state policy concerns renders it no less a rule of substantive law. See Stewart, Punitive Damages Arbitration: Fish or Cut Bait, N.Y.L.J., Feb. 21, 199 1, at 5, col. 1.

We emphasize that an agreement between the parties specifically to award punitive damages may well have dictated a different outcome. The Garrity rule, to the extent that it purports to prevent arbitrators from awarding punitive damages in the face of such an agreement seems to invoke preemption concerns, since it runs afoul of the federal substantive law rules that sweep aside any state attempt to interfere with the agreement of the parties. The matter may be left for another day, however, because we deal here only with the NYSE provisions for

arbitration.

Article XI of the NYSE Constitution provides that "[a]ny controversy between . . . a member, allied member or member organization and any other person, arising out of the business of such member . . . , shall at the instance of any such party, be submitted for arbitration . . . ." 2 N.Y.S.E. Guide (CCH) ¶ 1501. Additionally, NYSE rule 600(a) provides for the arbitration of "[a]ny dispute, claim or controversy," 2 N.Y.S.E. Guide (CCH) ¶ 2600, and NYSE rule 347 provides for the arbitration of "any controversy . . . arising out of the employment or termination of employment. . . " 2 N.Y.S.E. Guide (CCH) ¶ 2347.

Despite this broad language, the NYSE provisions are silent with regard to the power of arbitrators to award punitive damages. As the district court observed, unlike the cases involving arbitration agreements incorporating the rules of the American Arbitration Association ("AAA"), which provide that arbitrators may award "any remedy or relief which [is] just and equitable and within the scope of the agreement," see Bonar, 835 F.2d at 1386 (upholding AAA award of punitive damages); Raytheon Co. v. Automated Business Sys., Inc., 882 F.2d 6, 9 (1st Cir. 1989) (same), the NYSE rules have no provisions relating to remedy or relief. Clearly, if the NYSE wanted to empower arbitrators to award punitive damages, it could have done so. See Friedman, Punitive Damages in Securities Cases, N.Y.L.J., May 2, 1991, at 3, col. 1.

Waltman points to the award form, which is used by NYSE arbitrators to memorialize the arbitral awards and allows for entry of a punitive damages award under a specific heading marked "punitive damages," to support

his contention that NYSE arbitrators are empowered to award punitive damages. We cannot conclude that award forms are part of the arbitration agreement. Moreover, NYSE arbitrations occur throughout the nation, and our holding here does not mean that in those states in which arbitral punitive damages awards are permitted, arbitrators may not appropriately utilize the punitive damages section of the award form.

In a recent decision of this Court, the panel in dictum noted that "in an appropriate case, the arbitrators could enhance [an award] by punitive damages if prior misconduct established entitlement to such damages." Kerr-McGee Refining Corp. v. M/T Triumph, 924 F.2d 467, 470 (2d Cir. 1991) (citing Bonar, 835 F.2d at 1387). In Kerr-McGee, the plaintiff was awarded treble damages under the Racketeer Influenced and Corrupt Organizations ("RICO") Act, 18 U.S.C. §§ 1961-1968, in an arbitration proceeding. 924 F.2d at 469-70. Kerr-McGee, however, was not a diversity case requiring a preemption analysis, since RICO there provided federal question jurisdiction under 28 U.S.C. § 1331.

Although "[w]e have consistently accorded the narrowest of readings to the Arbitration Act's authorization to vacate awards," Andros Compania, 579 F.2d at 703, we also have noted that under Garrity an arbitral award of punitive damages must be vacated in an appropriate case. See John T. Brady & Co. v. Form-Eze Sys., Inc., 623 F.2d 261, 263 (2d Cir.) (" 'where the damages are genuinely intended to be punitive[,] . . . the courts [should] vacate the award' " (citation omitted)), cert. denied, 449 U.S. 1062 (1980); see also Synergy Gas Co. v. Sasso, 853 F.2d 59, 65-66 (2d Cir.) (dicta), cert. denied, 488 U.S. 994, (1988). For the reasons given, this is an appropriate case

under the provisions of section 10(d) of the FAA for vacatur of the punitive damages award.

CONCLUSION

The judgment of the district court is affirmed in all respects.

MAHONEY, Circuit Judge, concurring in part and dissenting in part:

I join the majority opinion insofar as it affirms that portion of the judgment below which confirmed the arbitral award of compensatory damages. I respectfully dissent, however, from the majority's affirmance of the district court's vacatur of the arbitral award of punitive damages.

The majority recognizes the fundamental requirement of the FAA "that parties comply with their agreements to arbitrate." They further concede that "the parties have not specified remedies and . . . the arbitrators therefore should be free to fashion appropriate relief." They deem these considerations outweighed, however, by the fact that diversity of citizenship provides the basis for federal jurisdiction in this case. This leads them to apply normally applicable diversity rules, and thus to conclude that the availability of punitive damages is a question of substantive law for which state law provides the rule of decision. Deeming New York law applicable, they then invoke Garrity v. Lyle Stuart, Inc., 40 N.Y.2d 354, 353 N.E.2d 793, 386 N.Y.S.2d 831 (1976), to affirm the district

court's vacatur of the arbitral award of punitive damages.

In my view, this analysis misreads the applicable law and creates an unnecessary conflict with two of our sister circuits. As the Supreme Court stated in Moses M. Cone Memorial Hosp. v. Mercury Constr. Corp., 460 U.S. 1 (1982):

> The Arbitration Act is something of an anomaly in the field of federal-court jurisdiction. It creates a body of federal substantive law establishing and regulating the duty to honor an agreement to arbitrate, yet it does not create any independent federal-question jurisdiction under 28 U.S.C. § 1331 (1976 ed., Supp. V) or otherwise. Section 4 provides for an order compelling arbitration only when the federal district court would have jurisdiction over a suit on the underlying dispute; hence, there must be diversity of citizenship or some other independent basis for federal jurisdiction before the order can issue.

Id. at 25 n.32 (emphasis added).

The majority's approach effectively disregards the existence of a "body of federal substantive law establishing and regulating the duty to honor an agreement to arbitrate," id., and imposes the diversity regime of Erie R.R. v. Tompkins, 304 U.S. 64 (1938). The Erie standard is intended, however, for "all matters except those in which some federal law is controlling." Id. at 72. It therefore, seems to me clearly inappropriate to apply Erie-generated rules to an area for which, the Supreme Court has instructed, federal law supplies the rule of decision. That,

however, is precisely what the majority has done in this case.

The Supreme Court has continually reiterated that the FAA "simply requires courts to enforce privately negotiated agreements to arbitrate, like other contracts, in accordance with their terms." Volt Information Sciences, Inc. v. Board of Trustees, 489 U.S. 468, 478 (1989). As the Court stated in Volt:

> The FAA was designed "to overrule the judiciary's long-standing refusal to enforce agreements to arbitrate," Dean Witter Reynolds Inc. v. Byrd, 470 U.S. [213, 219-20 (1985)], and to place such agreements " 'upon the same footing as other contracts,' " Scherk v. Alberto-Culver Co., 417 U.S. [506, 511 (1974)] (quoting H.R Rep. No. 96, 68th Cong., 1st Sess., 1, 2 (1924)). While Congress was no doubt aware that the Act would encourage the expeditious resolution of disputes, its passage "was motivated, first and foremost, by a congressional desire to enforce agreements into which parties had entered." Byrd, 470 U.S., at 220.

Id. Accordingly, the FAA mandates district courts, upon application, to "direct[ ] that . . . arbitration proceed in the manner provided for in [the parties'] agreement." 9 U.S.C. § 4 (1988) (emphasis added).

It follows that a state law which limits freedom of contract with respect to arbitration agreements covered by the FAA conflicts with the FAA and is preempted by it. See Saturn Distribution Corp. v. Williams, 905 F.2d 719, 722 (4th Cir.) ("with few imitations, if a state law singles out arbitration agreements and limits their enforceability

it is preempted."), cert. denied, 111 S. Ct. 516 (1990); cf. Volt, 489 U.S. at 479 ("Arbitration under the [FAA] is a matter of consent, not coercion, and parties are generally free to structure their arbitration agreements as they see fit.").

As a result, the cases that have addressed the question whether punitive damages may be awarded in arbitration have looked to the agreement between the parties to resolve the issue. See, e.g., Raytheon Co. v. Automated Business Sys., 882 F.2d 6, 9-12 (1st Cir. 1989); Bonar v. Dean Witter Reynolds, Inc., 835 F.2d 1378, 1386-88 (11th Cir. 1988); Pyle v. Securities U.S.A., Inc., 758 F. Supp. 638, 639 (D. Colo. 1991); Barbier v. Shearson Lehman Hutton, Inc., 752 F. Supp. 151, 159-60 (S.D.N.Y. 1990); Peabody v. Rotan Mosle, Inc., 677 F. Supp. 1135, 1139 (M.D. Fla. 1987); Ehrich v. A.G. Edwards & Sons, Inc., 675 F. Supp., 559, 563 (D.S.D. 1987); Duggal Int'l, Inc. v. Sallmetall, B.V., No. 84 Civ 7170 (JMC) (S.D.N.Y. May 8, 1986); Willoughby Roofing & Supply Co. v. Kajima Int'l, Inc., 598 F. Supp. 353, 357-59 (N.D. Ala. 1984), aff'd, 776 F. 2d 269 (11th Cir. 1985) (per curiam); Willis v. Shearson/American Express, Inc., 569 F. Supp. 821, 823 (M.D.N.C. 1983).

Further, as the majority recognizes, courts have rebuffed efforts to invoke Garrity to preclude an arbitral award of punitive damages even where the pertinent contract explicitly stated that it was to be governed by New York law. See, e.g., Bonar, 835 F.2d at 1386-87; Barbier, 752 F. Supp. at 153, 160 & n.15; Singer v. E.F. Hutton & Co., 699 F. Supp. 276, 278-79 (S.D. Fla. 1988); Duggal Int'l, slip op. at __, __ n.4; Willis, 569 F. Supp. at 823-24; see also Raytheon, 882 F.2d at 11 (rejecting Garrity),

Ehrich, 675 F. Supp. at 565 (same); Willoughby, 598 F. Supp. at 359 (same).

If an express provision that a contract will be governed by New York law does not suffice to render an arbitration under that contract subject to Garrity, it must surely follow a fortiori that the mere invocation of diversity jurisdiction does not do so. Further, the imposition of the Garrity rule, without respect to (or any meaningful inquiry regarding) the contractual intention of the parties, directly contravenes the dominant purpose and policy of the FAA as repeatedly articulated by the Supreme Court.

The district court herein ruled that because Garrity "is not in direct conflict with any express provision of the [FAA]," it should be invoked to preclude any award of punitive damages. Fahnestock & Co. v. Waltman, No. 90 Civ. 1792 (PKL), slip op. at 10 (S.D.N.Y. Aug. 23, 1990). Although the contract at issue was distinguished from contracts incorporating an American Arbitration Association rule that is often read to authorize an award of punitive damages, id. at 11, no significant inquiry was conducted regarding the intent of the parties, and no mention was made of the NYSE award form, applicable here, that makes specific provision for punitive damages. Rather, Garrity was deemed controlling as a matter of law.

In affirming, my colleagues dismiss the award form because they "cannot conclude that award forms are part of the arbitration agreement." Indeed, in the absence of any consideration of the issue by the district court, it is impossible on this record to reach any conclusion pro or con regarding the matter, or more generally regarding the intent of the parties as to the award of punitive damages.

The majority makes clear, in any event, that it "might" defer only to an explicit agreement between the parties authorizing an award of punitive damages.

Given the rule that "ambiguities as to the scope of the arbitration clause [are] resolved in favor of arbitration," Volt, 489 U.S. at 476; see also Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, 473 U.S. 614, 626 (1985) ("as with any other contract, the parties' intentions control, but those intentions are generously construed as to arbitrability."); Moses M. Cone, 460 U.S. at 24-25 ("any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration"), a much more hospitable approach to arbitral power to award punitive damages is appropriate. In any event, some significant inquiry as to contractual intent is required. Clearly, none has occurred here.

I would therefore reverse the ruling of the district court vacating the arbitral award of punitive damages and remand for reconsideration of that issue in terms of the contractual intent of the parties. I am not prepared to conclude at this juncture that the outcome of that necessarily particularized inquiry will result in a different outcome on this issue. I am convinced, however, that the inquiry should be undertaken, rather than aborted by the invocation of Garrity.

No precedent of this court calls for a different result. John T. Brady & Co. v. Form-Eze Systems, Inc., 623 F.2d 261, 263-64 (2d Cir.), cert. denied, 449 U.S. 1062 (1980), discussed Garrity, but concluded that no award of punitive damages had been made requiring any ruling on the issue in that case. Synergy Gas Co. v. Sasso, 853 F.2d 59, 65 (2d Cir.), cert. denied, 488 U.S. 994 (1988),

similarly dismissed an argument premised upon Garrity because the arbitral award was construed not to include punitive damages. Accordingly, neither case had any occasion to address the issue whether Garrity can operate to preclude punitive damages awards in FAA arbitrations. In any event, any ruling giving that effect to Garrity would be inconsistent with Moses M. Cone's teaching that the FAA "creates a body of federal substantive law establishing and regulating the duty to honor an agreement to arbitrate." 460 U.S. at 25 n. 32. More recently, in Kerr-McGee Refining Corp. v. M/T Triumph, 924 F.2d 467, 470 (2d Cir. 1991), we stated, in the context of an arbitration of a RICO claim, that punitive damages could be awarded "in an appropriate case," citing Bonar.

Although our precedents are ambiguous, I conclude that governing Supreme Court doctrine, the vast weight of federal court authority on the issue, and basic principles of federal arbitration law counsel against the ruling of the majority in this case on the issue of punitive damages. I therefore respectfully dissent from that ruling.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

In the Matter of The New York Stock Exchange Arbitration Between	: 90 Civ. 1792 (PKL)
FAHNESTOCK & CO., INC.	Opinion & Order
Petitioner,	
-against-	
JOSEPH J. WALTMAN,	
Respondent.	

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LEISURE, District Judge:

This action was brought by petitioner Fahnestock and Co., Inc. ("Fahnestock") to vacate an arbitration award rendered by the New York Stock Exchange, pursuant to the Federal Arbitration Act, 9 U.S.C. § 10. The arbitrators awarded damages to respondent Joseph J. Waltman ("Waltman") for defamation and wrongful termination of employment by Fahnestock. Fahnestock seeks to vacate this award on the grounds that the arbitrators exceeded their power by ignoring certain policies of the New York Stock Exchange, Inc. ("NYSE") and National Association of Securities Dealers, Inc. ("NASD"), and by rendering an award of punitive damages. Respondent seeks to dismiss this petition pursuant to Fed. R. Civ. P. 12 (b) (3) and 12 (b) (6) , or in the alternative, to transfer the action to the United States District Court for the Eastern District of Pennsylvania, pursuant to 28 U.S.C. § 1410(a).

BACKGROUND

Fahnestock is a securities corporation with its principal place of business in New York. On March 16, 1982, Fahnestock hired defendant Waltman as an at-will employee, to serve in the capacity of a "registered representative to head Fahnestock's Retirement Trust Division and thereafter, at Fahnestock's request, to manage and build Fahnestock's insurance products business." Petition to Vacate, ¶ 5. Waltman was based in New York and Pennsylvania. In addition to his work with Fahnestock, Waltman, in 1985, established a general insurance agency in Pennsylvania for the purpose of marketing insurance and annuity products in

Pennsylvania and other states, in connection with Keystone Providence Live Insurance Company. On December 12, 1988, Fahnestock notified Waltman that his employment with the company had been terminated, and subsequently, filed a Uniform Termination Statement ("Form U-5") with the National Association of Securities Dealers to record Waltman's discharge. Petition to Vacate, Exhibit A. Fahnestock was later allegedly unable to locate certain insurance files, and believed that, since Waltman had been responsible for the files, he had retained them. Fahnestock, therefore, requested that the files be returned. Waltman, however, contended that the files in question were materials which were used in connection with his general insurance agency. Waltman then supplied Fahnestock with a list of account executives about which the files he retained were concerned, and offered to make available the information contained in the files, in return for the release and indemnification of Waltman against any and all claims. Respondent's Memorandum of Law, Exhibit A. Fahnestock, instead of complying with Waltman's request, filed a statement of claim with the Arbitration Department of the New York Stock Exchange on January 27, 1989, requesting investigation of the matter. Petition to Vacate, Exhibit B. Subsequently, Fahnestock filed an amended Form U-5 noting the commencement of the arbitration, and that Waltman was under "internal review for fraud or wrongful taking of property, or violating investment related statutes, regulations, rules or industry standards of conduct." Petition to Vacate, Exhibit C.

Waltman, on March 20, 1989, served an answer and counterclain in the New York Stock Exchange arbitration, in which he denied Fahnestock's allegations and

maintained that he had been wrongfully terminated. In addition, Waltman alleged that Fahnestock and three individually named defendants the Chairman of the Board, the President, and the General Counsel of Fahnestock -- had defamed him by filing the amended Form U-5 with the National Association of Securities Dealers. Waltman alleged that Fahnestock participated in needless and malicious harassment which "resulted in a permanent record of alleged misconduct through Fahnestock's filing of an amended U-5 with the NASD after it filed its claim against him." Respondent's Memorandum of Law, p. 2. On January 19, 1990 the arbitrators rendered their decision, and awarded $56,000.00 to Waltman in compensatory damages, in addition to $14,000.00 for legal fees, $100,000.00 for defamation in filing the amended Form U-5, and $100,000.00 in punitive damages. Petition to Vacate, Exhibit E. Waltman then filed a petition in the United States District Court for the Eastern District of Pennsylvania to confirm and enter judgment on the arbitration award, pursuant to New York Stock Exchange Arbitration Rule 628(a). On March 15, 1990 Fahnestock filed the instant petition to vacate the award of the arbitrators pursuant to 9 U.S.C. § 10, alleging that the

arbitrators "exceeded their powers"[1] by rendering a defamation award and by awarding punitive damages. Judge J. William Ditter, Jr., United States District Judge for the Eastern District of Pennsylvania rendered a decision dated May 22, 1990, staying the petition to confirm the award of the arbitrators "pending the outcome of [Fahnestock's] petition to vacate, filed in the Southern District of New York." Petitioner's Reply Memorandum, Exhibit A. Respondent, in response, has filed a motion to dismiss for improper venue, or in the alternative, to transfer the instant action to the Eastern District of Pennsylvania.

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[1] The Federal Arbitration Act, 9 U.S.C. § 10, provides that an arbitration award may be vacated:

(a) Where the award was procured by corruption, fraud, or undue means.
(b) Where there was evident partiality or corruption in the arbitrators, or either of them.
(c) Where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced.
(d) Where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made.

DISCUSSION

A. Petitioner's Motion to Vacate the Arbitration Award

Petitioner seeks vacatur of the arbitration award maintaining that the arbitration committee exceeded its power by disregarding the law with respect to certain New York Stock Exchange and National Association of Securities Dealers regulations, and with respect to the privilege afforded any discharge of a public or private duty, attached thereto. Fahnestock also maintains that the arbitrators disregarded the legal privilege imparted to all statements made in the course of a judicial or quasi-judicial proceeding, which would protect the statement of claim against Waltman as filed by Fahnestock. In addition, Fahnestock argues, the arbitration panel exceeded its power by granting an award of punitive damages. It is a well established principal that "arbitrators may render a lump sum award without disclosing their rationale for it, and that when they do, courts will not inquire into the basis of the award unless they believe that the arbitrators rendered it in 'manifest disregard' of the law . . ." Koch Oil S.A. v. Transocean Gulf Oil Co., 751 F.2d 551 (2d Cir. 1985) (citing Kurt Orban Co. v. Angeles Metal Systems, 573 P.2d 739, 740 (2d Cir. 1978)). The "manifest disregard" doctrine was judicially created by the Supreme Court in Wilko v. Swan, 346 U.S. 427 (1953), as an extension of 9 U.S.C. § 10(d) which provides for vacatur of an arbitration award upon a showing that the arbitrators "exceeded their powers." The doctrine is "extremely limited", and hence, the court is "not at liberty to set aside an arbitration panel's award because of an arguable difference regarding the meaning or applicability of laws

urged upon it." Merrill Lynch, Pierce, Fenner, and Smith, Inc. v. Bobker, 808 F.2d 930; 934 (2d Cir. 1986). See also Reynolds Secur., Inc. v. Macquown, 459 F.Supp. 943, 945 (W.D.Pa. 1978). This standard "presupposes something beyond and different from a mere error in the law or failure on the part of arbitrators to understand or apply the law." Saxis Steamship Co. v. Multifacs International Traders, Inc., 375 F.2d 577, 582 (2d Cir. 1967) (citing San Martine Companie de Maregacion v. Sagueray Terminal Ltd., 293 F.2d 796, 801 (9th Cir. 1961)). See also Synergy Gas Co. v. Sasso, 853 F.2d 59 (2d Cir.), cert. denied, 109 S. Ct. 559 (1988). Thus, the complaining party must prove that the arbitrators "understood and correctly stated," yet completely ignored the law, in order to establish that an arbitration award should be vacated on the grounds of "manifest disregard." Id.

In the instant case, petitioner maintains that the arbitration committee disregarded the NASD and NYSE regulations which require that an amended Form U-5 be filed in the event that any inaccuracies develop in the original Form U-5. Fahnestock argues that it was obligated to disclose the commencement of Waltman's investigation regarding "possible fraud or wrongful taking" of the insurance files in question, and that since the arbitrators were aware of this obligation and nonetheless granted the defamation award, manifest disregard is obvious.

The Court has conducted a thorough complete review of the entire record, and is unable to conclude that the arbitrators exceeded their power by ignoring the NASD and NYSE regulations. The arbitrators considered the regulations, as evidenced in the transcript of the

arbitration proceedings, and rendered a decision based on their interpretation of the regulations. Furthermore,, according to the "manifest disregard" standard for vacatur, the Court is not empowered to set aside the decision of the arbitration committee because of disagreement about the interpretation of the regulations at issue. Nor may the Court inquire into the rationale of the arbitrators in rendering the award.

Petitioner also argues that the filing of the amended Form U-5 was protected by an absolute privilege which is afforded to any discharge of a public or private duty. The Court has reviewed the relevant caselaw presented by petitioner, and concludes that a detailed examination of the law reveals that such privilege is not absolute, and may be overcome by a showing of malice. For example, in Greenfield v. Kanwit, 546 F.Supp. 220 (S.D.N.Y.), aff'd without op., 714 F.2d 113 (2d Cir. 1982), the Court recognized that "New York extends a common law privilege to any communication made in discharge of a private or public duty, whether legal or moral." 546 F.Supp. at 227 (citing Shapiro v. Health Ins. Plan. of Greater New York, 7 N.Y.2d 56, 194 N.Y.S.2d 509, 163 N.E.2d 333 (1959)). The court, however, concluded that such privilege is not absolute and "may be (overcome by a showing that the statement: was motivated or actuated by actual malice." Id. (citing Perfect Fit Industries v. Acme Quilting Co., 494 F.Supp. 505 (S.D.N.Y. 1980)). Therefore, in the instant case, although the filing of the amended Form U-5 can be interpreted as the discharge of a private duty and is thus privileged, the arbitrators may have concluded that the privilege was overcome by the existence of actual malice. A finding of malice is an issue of fact and, therefore, unreviewable on a motion to vacate.

Petitioner also maintains that the arbitrators ignored the governing legal principal with respect to the absolute privilege which is imparted to any communication made in light of a judicial or quasi-judicial proceeding. Fahnestock contends that the filing of the statement of claim enjoyed such privilege as a pleading in a quasi-judicial proceeding. A closer examination of the relevant caselaw presented by petitioner in support of this proposition also reveals that such privilege is not absolute and may be overcome by a showing of malice or lack of probable cause. The privilege was discussed in Lewis v. Elliott, 628 F.Supp. 512 (D.D.C. 1986), a defamation action based on an "allegedly defamatory publication contained in affidavit attached to a bid protest letter," brought by a federal employee against two corporations. Id. Although the court recognized that statements made prior to or in the course of a judicial or quasi-judicial proceeding are absolutely privileged, and that such proceedings include arbitration proceedings, Id. at 516 (citing Sturdivanet v. Seaboard Service System, Ltd., 459 A.2d 1058, 1060 (D.C. App. 1983)), the court concluded that such statements are privileged "only if it appears that the affiant had probable cause to make the affidavit. Id. at 517, (citing King v. Hildebrandt, 331 F.2d 476 (2d Cir. 1964). See also Youmans v. Smith, 153 N.Y. 214, 47 N.E. 265 (1897). Similarly, in Meyers v. Amerada Hess Corp., 647 F.Supp. 62 (S.D.N.Y. 1986), the court recognized that the privilege can be waived if abused. The court reasoned that the "accepted standard for determining whether there has been an abuse of the privilege requires the court to determine whether the statements are 'so obviously impertinent as not to admit of discussion, and so needlessly defamatory as to warrant the inference of express malice'." Id., at 65-66 (quoting Youmans v. Smith, 153 N.Y. 214, 220, 47 N.E. 265 (1897)).

The Court concludes that a showing of actual malice or lack of probable cause can overcome the privilege afforded to communications made in a quasi-judicial proceeding. As previously discussed, the existence of actual malice is a question of fact and the Court may not inquire into the rationale of the arbitration committee in rendering the award. Thus, the arbitration committee may indeed have determined that a waiver of the privilege was appropriate in the instant case.

Fahnestock also argues that the arbitration panel exceeded its power in rendering an award of punitive damages to Waltman and that therefore, this portion of the award should be vacated. Fahnestock argues that, under New York law, an arbitration panel is not empowered to grant punitive damages. Garrity v. Lyle Stuart, Inc., 40 N.Y.2d 354, 386 N.Y.S.2d 831, 353 N.E.2d 793 (1976). In Garrity, the New York Court of Appeals held that "an arbitrator has no power to award punitive damages, even if agreed upon by the parties." Id. at 832. The court reasoned that "enforcement of an award of punitive damages as a purely private remedy would violate public policy . . .", and thus, any such award imposed by an arbitrator should be vacated. Id. at 356-57.

Respondent maintains that federal substantive law governs any arbitration conducted pursuant to the Federal Arbitration Act, and therefore, an award of punitive damages is appropriate. In support of this proposition, respondent relies on the United States Supreme Court decision in Southland Corp. v. Keating, 465 U.S. 1 (1984). In Southland, the Court determined that any state law which is in direct conflict with the Federal Arbitration Act is violative of the Supremacy Clause of the United States Constitution. The Court explained that "[t]he

Arbitration Act 'creates a body of federal substantive law' . . . applicable in state and federal courts. Id. at 12 (quoting Moses H. Cone Memorial Hospital v. Mercury Construction Corp., 460 U.S. 1, 25 n.32 (1983). In the instant case, however, the state substantive law as set forth in Garrity v. Lyle Stuart, Inc. regarding the inability of arbitrators to award punitive damages, is not in direct conflict with any express provision of the Federal Arbitration Act. Therefore, the Supreme Court's decision in Southland is not determinative of the issue before the Court.

Respondent also draws the Court's attention to certain decisions which are inconsistent with that of Garrity, and allow arbitrators to award punitive damages. The Court notes, however, that respondent's reliance on these cases is misplaced. Two of the cases relied upon reflect the positions of the First and Eleventh Circuits, and are therefore not controlling authority. See Raytheon Co. v. Automated Business Systems, Inc., 882 F.2d 6 (1st Cir. 1989); Bonar v. Dean Witter Reynolds, Inc., 835 F.2d 1378 (11th Cir. 1988). In Dugall International, Inc. v. Sallmetall, No. 84 Cir. 7170 (S.D.N.Y. 1986), Judge John M. Cannella of this Court found Garrity inapplicable to an arbitration whose confirmation was sought under the Federal Arbitration Act. First, the Court notes that all the cases relied upon by respondent, including Dugall, are distinguishable upon closer examination from the circumstances of the instant case, as the arbitration agreements in those cases incorporate the rules of the American Arbitration Association which provide for an arbitration panel's award of "any remedy or relief which is just and equitable and within terms of the agreements of the parties," AAA Rules, Rule 43, including punitive damages. In this case, no such provision was part of the

arbitration agreement. Further, to the extent that Dugall can be read as a general rejection of Garrity, this Court declines to follow it as inconsistent with existing law.

The Second Circuit has implicitly, yet consistently, affirmed the Garrity decision in determining whether punitive damages were appropriate. For example, in John T. Brady & Co. v. Form-Eze Systems, Inc., 623 F.2d 261 (2d Cir.), cert. denied, 449 U.S. 1062 (1980), the court allowed an arbitration panel to grant an award which was not explicitly punitive and was provided for in the arbitration agreement. The Brady Court found that damages not clearly punitive in nature should not be vacated under Garrity. However, the Court implicitly upheld Garrity, stating that "[o]nly where the damages are intended to be punitive should the Court vacate the award." Id. at 264. See also Synergy Gas Co. v. Sasso, 853 F.2d 59 (2d Cir. 1988); Sweeney v. Morganroth, 451 F.Supp. 367 (S.D.N.Y. 1978); O'Driscoll, et al. v. Merrill Lynch, Pierce, Fenner & Smith, Inc., [1984-85 Transfer Binder] Fed.Sec.L.Rep. (CCH) para. 91, 822 at p. 90, 134 (S.D.N.Y. Oct. 26, 1984). Thus, in light of the precedent set forth by the Second Circuit, the Court concludes that in the instant case, the arbitration panel's award of punitive damages must be vacated.

B. Respondent's Motion to Dismiss for Improper Venue, or to transfer to the Eastern District of Pennsylvania

Respondent has moved to dismiss the action for improper venue, or in the alternative, to transfer the action to the Eastern District of Pennsylvania. Since the cause of action arose in this District and petitioner resides

in New York, venue in this District is proper. 28 U.S.C. § 1391(a).

Sections 9, 10, and 11 of the Federal Arbitration Act provide the procedures for confirming, vacating or modifying an arbitration award. These sections, however, "leave open for interpretation the question of where a dispute over an arbitration award is properly venued when plaintiff and defendant have moved in different forums to confirm and vacate the award." J.V.B. Industries v. Federated Dept. Stores, Inc., 684 F.Supp. 22, 23 (E.D.N.Y. 1988). Therefore, certain factors must be considered before determining whether transfer is appropriate.

Either party in an action brought in federal district court may move to have it transferred to another federal district court where the action could have been brought originally. Such motions for transfer are made pursuant to 28 U.S.C. § 1404(a), which provides:

> For the convenience of the parties and witnesses, in the interests of justice, a district court may transfer any civil action to any other district or division where it might have been brought.

A motion to transfer pursuant to this section rests with the sound discretion of the Court. Heller Financial, Inc. v. Midwhey Powder Co., 883 F.2d 1286, 1293 (7th cir. 1989); Golconda Mining Corp. v. Herlands, 365 F.2d 856, 857 (2d Cir. 1966). The party requesting transfer "bears the burden of proof and that burden must be carried by a preponderance of the evidence." In Re Manville Forest Products Corp., 896 F.2d 1384, 1390 (2d Cir. 1990);

Morales v. Navieras De Puerto Rico, 713 F.Supp. 711, 712 (S.D.N.Y. 1989). A number of factors are relevant to a court's determination of a transfer motion, among which are the convenience of the parties, the ease of access to the sources of proof, the susceptibility of the witnesses to process, and the interests of justice. Nieves v. American Airlines, 700 F.Supp. 769 (S.D.N.Y. 1988).

The threshold question in a transfer motion is whether the action could have been brought in the district to which transfer is proposed. Wright, Miller & Cooper, Federal Practice and Procedure § 1391. In a diversity action, venue is proper in the judicial district where all defendants reside, where all plaintiffs reside, or where the claim arose, 28 U.S.C. § 1391(a). Respondent resides in the Eastern District of Pennsylvania, and thus venue would be proper in the proposed transferee court.

Respondent has presented the Court with a myriad of reasons why such a transfer is appropriate. Primarily, respondent argues that petitioner agreed to submit to jurisdiction of the respondent's choice by voluntarily requesting arbitration to decide the instant matter.[2]

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[2] Rule 628(a) of the Arbitration Rules of the New York Stock Exchange provides:

> All awards shall be in writing and signed by a majority of the arbitrators or in such manner as is required by law. Such awards may be entered as a judgment in any court of competent jurisdiction.

Although the Court believes that it would have been procedurally preferable for petitioner to have brought this petition to vacate the arbitration award as a counterclaim to respondent's original petition to confirm in the Eastern District of Pennsylvania, the Court is unconvinced that this is a sufficient reason for transfer. Respondent maintains that, according to recent Second Circuit decisions "where there are two competing lawsuits, the first should have priority, absent the showing of a balance of convenience in favor of the second action, or unless there are special circumstances which justify giving priority to the second." Fort Howard Paper Co. v. William D. Witter, Inc., 787 F.2d 784, 790 (2d Cir. 1987). However, this Court has determined on a number of occasions, that venue is not necessarily dictated by "the race" to the Courthouse. Great American Insurance Co., 735 F.Supp. 581, 585-86 (S.D.N.Y. 1990). See also Motion Picture Laboratory Technicians Local 780 v. McGregor & Werner, Inc., 804 F.2d 16 (2d Cir. 1986); J.V.B. Industries, Inc., supra. Moreover, the Federal Arbitration Act provides for a motion to vacate in the district where the award was rendered. Since the award was made in this district, venue is proper here.

Respondent further argues that, since there are no witnesses involved, the convenience of the parties is of major concern. Transfer is appropriate, respondent maintains, because petitioner has far greater financial size and capacity, and thus, should be the party to bear the cost of suit in a distant forum. It is true that a court can consider the relative means of the parties in reaching a decision on a motion for transfer. See, e.g., Goldstein v. Rusco Industries, Inc., 351 F.Supp. 1314, 1318 (E.D.N.Y. 1972). However, as respondent emphasizes, "this is the type of matter that is going to be heard on briefs and

notes of testimony alone," and thus, the Court concludes that pursuing the instant action in this District would not be unduly burdensome. Given that the documents have already been filed in this Court, the balance of convenience weighs in favor of retaining the action in this District. Furthermore, respondent's argument reduces to a desire to shift the cost of pursuing a distant action to petitioner. It is elemental that a mere shifting of inconveniences is not grounds for transfer. Finkielstain v. Seidel, 692 F.Supp. 1497, 1509-10 (S.D.N.Y. 1988), aff'd in part and rev'd in part, 857 F.2d 893 (2d Cir. 1988).

Finally, respondent maintains that transfer is necessary since respondent lives in Pennsylvania and conducted business for Fahnestock in Pennsylvania. In consideration of all factors involved in the present case, however, the Court concludes that the balance weighs in favor of retaining this action in this District. Respondent was based in New York, as well as in Pennsylvania, in connection with his business with Fahnestock. Petitioner's principal place of business is in New York, and the arbitration took place in New York. The action's only substantial connection with Pennsylvania is that respondent resides there. Thus, respondent has failed to meet his burden of persuading the Court that transfer is warranted. Accordingly, respondent's motions to dismiss for improper venue and to transfer the instant action to the Eastern District of Pennsylvania are denied.

CONCLUSION

For the reasons set forth above, petitioner's motion to vacate the arbitrator's award for defamation is denied. Petitioner's motion to vacate the arbitrator's award of punitive damages is granted. Respondent's motion to dismiss and to transfer to the Eastern District of Pennsylvania are denied.

SO ORDERED Dated: August 22, 1990
New York, New York

/s/ Peter K. Leisure
U.S.D.J.

RELEVANT STATUTORY AND CONSTITUTIONAL PROVISIONS

United States Constitution, Article VI

Clause 2. Supreme Law.

This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.

Title 9 U.S.C.

§ 2. Validity, irrevocability, and enforcement of agreements to arbitrate

A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

July 30, 1947, c. 392, 61 Stat. 670.

§ 10. Same; vacation; grounds; rehearing

In either of the following cases the United States court in and for the district wherein the award was made may make an order vacating the award upon the application of any party to the arbitration --

(a) Where the award was procured by corruption, fraud, or undue means.

(b) Where there was evidence partiality or corruption in the arbitrators, or either of them.

(c) Where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced.

(d) Where the arbitrators exceeded their powers, or so imperfectly executed them, that a mutual, final and definite award upon the subject matter submitted was not made.

(e) Where an award is vacated and the time within which the agreement required the award to be made has not expired the court may, in its discretion, direct a rehearing by the arbitrators.

July 30, 1947, c. 392, 61 Stat. 672.

NEW YORK STOCK EXCHANGE ARBITRATION PROVISIONS AND RULES

ARTICLE XI, SECTION 1 OF THE NYSE CONSTITUTION

Controversies Arbitrated. Any controversy between parties who are members, allied members or member organizations and any controversy between a member, allied member or member organization and any other person arising out of the business of such member, allied member or member organization, or the dissolution of a member organization, shall at the instance of any such party, be submitted for arbitration in accordance with the provisions of this Constitution and such rules as the Board may from time to time adopt.

ARBITRATION RULE 347. Controversies as to Employment or Termination of Employment

> Any controversy between a registered representative and any member or member organization arising out of the employment or termination of employment of such registered representative by and with such member or member organization shall be settled by arbitration, at the instance of any such in accordance with the arbitration procedure prescribed elsewhere in these rules.

ARBITRATION RULE 600. Arbitration

(a) Any dispute, claim or controversy between a customer or non-member and a member, allied member,

member organization and/or associated person arising in connection with the business of such member, allied member, member organization and/or associated person in connection with his activities as an associated person shall be arbitrated under the Constitution and Rules of the New York Stock Exchange, Inc. as provided by any duly executed and enforceable written agreement or upon the demand of the customer or non-member.

(b) Under this Code, the New York Stock Exchange, Inc., shall have the right to decline the use of its arbitration facilities in any dispute, claim or controversy, where -- having due regard for the purposes of the New York Stock Exchange, Inc. and the intent of this Code -- such dispute, claim or controversy is not a proper subject matter for arbitration.

FILED
JAN 9 1992
OFFICE OF THE CLERK

No. 91-699

IN THE

Supreme Court of the United States

OCTOBER TERM, 1991

JOSEPH J. WALTMAN,

Petitioner,

vs.

FAHNESTOCK & CO., INC.,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

RESPONDENT'S BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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OPINION BELOW

The Respondent, Fahnestock & Co., Inc. ("Fahnestock"), respectfully urges this Court to deny the Petition of Joseph J. Waltman ("Waltman") for a writ of certiorari, to review the decision of the United States Court of Appeals for the Second Circuit in this case.* That

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*- If this Court grants the instant Petition, the Respondent urges this Court to simultaneously reconsider the question presented in Fahnestock's prior Petition for a writ of certiorari filed on September 9, 1991, Index No. 91-508, and previously denied by this Court on November 4, 1991 based upon the subsequent publication of a decision by New York's Appellate Division. In Herzfeld & Stern v. Beck, 572 N.Y.S.2d 683 (1st Dept. 1991), New York's Appellate Division made it clear that as Fahnestock contended, relevant statements made in a mandated filing are absolutely privileged. Fahnestock's Petition sought review of the Second Circuit's opinion on the question of whether statements made in filings mandated by regulatory authorities were absolutely privileged. Waltman's Petition seeks review of that portion of the Second Circuit opinion dealing with the issue of punitive damages.

opinion is reported at 935 F.2d 512 (1991).

JURISDICTION

This Court has jurisdiction pursuant to Title 28 U.S.C. 1254(1).

STATUTES INVOLVED

The Federal Arbitration Act, Title 9 U.S.C. 10.

PROCEDURAL HISTORY

The origin of this matter is an NYSE arbitration between Fahnestock and its former employee, Joseph Waltman. Fahnestock initiated that proceeding in January 1989 seeking to recover certain files it believed Waltman wrongfully retained after his termination. Waltman filed a counterclaim in that proceeding against Fahnestock, its chairman, president and general counsel, alleging, inter alia, wrongful discharge and

defamation.

At the conclusion of the hearings, conducted entirely in New York, the arbitrators rendered an award (the "Award") dismissing Fahnestock's claim for recovery of its files and dismissing Waltman's claims against Fahnestock's chairman, president and general counsel. However, the arbitrators granted Waltman compensatory, defamation and punitive damages as against Fahnestock.

Invoking diversity jurisdiction (although he had worked out of Fahnestock's New York office, Waltman was a resident of Pennsylvania and Fahnestock was a New York corporation), Fahnestock thereafter filed a Petition with the United States District Court for the Southern District of New York seeking to vacate the Award to the extent it rendered an award for

defamation and granted punitive damages. In substance, Fahnestock argued that the arbitrators had exceeded their powers and ignored the law in rendering an award for defamation based upon Fahnestock's filing of a post-termination form mandated by the NASD. Fahnestock argued that relevant statements made in such regulatory filings were protected by an absolute privilege. Fahnestock also contended that the arbitrators exceeded their powers in rendering an award for punitive damages.

Fahnestock's Petition was granted in part and denied in part in an Opinion and Order of the United States District Court for the Southern District of New York (Judge Peter K. Leisure) dated August 22, 1990. Judge Leisure found that the arbitrators had exceeded their powers in rendering an award of punitive

damages, and, accordingly, vacated that portion of the Award.

Fahnestock timely appealed from that portion of the District Court's decision which refused to vacate the Award for defamation. Waltman cross-appealed from that portion of the decision which vacated the Award of punitive damages.

By decision dated June 10, 1991, the Second Circuit Court of Appeals affirmed the District Court's decision in all respects. Thereafter, Fahnestock timely filed a Petition for a writ of certiorari seeking to have this Court review that portion of the Second Circuit's decision as to the privilege applicable to statements made in mandated filings. That Petition was denied by this Court on November 4, 1991. The instant Petition by Waltman now seeks to have this Court review that portion of the Second Circuit's decision

which affirmed the District Court's vacatur of the award of punitive damages.

STATEMENT OF THE FACTS

Fahnestock is a member of the New York Stock Exchange ("NYSE"), engaged in business as a full-service stock brokerage firm with its principal place of business in New York City. In or about March 1982, Fahnestock employed Petitioner Waltman as a registered representative working primarily out of its New York offices. Fahnestock later requested that Waltman undertake to manage and build Fahnestock's insurance business and that he oversee the licensing of its salesmen and the sale of its insurance and annuity products. Waltman was employed by Fahnestock as an employee at will, there being no written employment agreement between Waltman and

Fahnestock.

On or about December 12, 1988, Waltman's employment was terminated by Fahnestock. In connection with that termination, and as required by the rules and regulations of the NYSE and the NASD, on or about January 4, 1989, Fahnestock filed a Uniform Termination Statement (a preprinted form prescribed by the NASD and more commonly referred to as "Form U-5") disclosing Waltman's termination.

Thereafter, Fahnestock discovered that its insurance files, including those relating to the insurance licensing of its registered representatives, were not to be found on Fahnestock's New York premises. Believing that Waltman possessed the missing files, Fahnestock contacted Waltman and requested that he return such files. Waltman, however, contended

that the files belonged to him. Accordingly, a dispute arose over the ownership and possession of such files.

Failing in efforts to amicably resolve that dispute, on or about January 27, 1989, Fahnestock filed a Statement of Claim with the Arbitration Department of the NYSE seeking the return of those files. That claim alleged solely that Waltman had wrongfully taken Fahnestock's files and sought an order directing their return. Shortly after the filing of its Statement of Claim, and again in accordance with the rules and regulations of the NYSE and NASD, Fahnestock also filed an Amended Form U-5, changing only one "NO" answer to a "YES" answer so as to truthfully disclose its dispute with Waltman.

More specifically, Question 15 on the printed Form U-5 asks:

	Yes	No
15. Currently, or at termination, was the individual under internal review for fraud or wrongful taking of property, or violating investment-related statutes, regulations, rules or industry standards of conduct?...	☐	☐

While Fahnestock had checked the "NO" box on the Form U-5 filed at the time of Waltman's termination, on or about February 2, 1989, Fahnestock amended that filing by checking the "YES" box in response to Question 15. No other changes were made on the Form U-5.

On or about March 20, 1989, Waltman served an answer in the NYSE arbitration and counterclaimed against Fahnestock, its chairman, president and general counsel. Waltman denied Fahnestock's allegations and asserted, by way of counterclaims, in pertinent part, his wrongful termination and that Fahnestock

had defamed him in filing the Amended U-5.

On or about January 19, 1990, the arbitrators rendered their Award. Contrary to the statements contained in Waltman's present Petition, the arbitrators clearly did not find that Waltman had proved that Fahnestock's chairman had threatened Waltman with arrest if he did not return Fahnestock's files or that Fahnestock's chairman had directed that the Amended U-5 be filed in such a way as to indicate that Waltman had been fired for cause. If anything, the opposite was true, for although the arbitrators heard contradictory testimony on these points, the arbitrators in their Award specifically dismissed all of Waltman's counterclaims against Fahnestock's chairman, its president and general counsel. Similarly, although Waltman's

Petition seeks to imply to the Court that the arbitral Award was based on Fahnestock's alleged course of conduct in attempting to damage Waltman's career, the Award itself makes no such statement and characterizes Waltman's counterclaims as merely being a claim for defamation arising from the filing of the Amended U-5.

Upon receiving the Award, Fahnestock commenced this challenge believing the arbitrators to have ignored the law as to the absolute privilege that applies to statements made in mandated filings, and believing the arbitrators to similarly have ignored New York law prohibiting arbitrators from rendering punitive damage awards absent a contractual agreement to present such issues to arbitration.

REASONS TO DENY THE WRIT

I. THIS COURT HAS PREVIOUSLY DECIDED THAT FEDERAL SUBSTANTIVE LAW DOES NOT PREEMPT THE ENTIRE FIELD OF ARBITRATION AND HAS ALSO PREVIOUSLY DECIDED THAT IN DIVERSITY CASES, THE PROPRIETY OF AN AWARD OF PUNITIVE DAMAGES IS A QUESTION OF STATE LAW

PRELIMINARY STATEMENT

Contrary to the impression Waltman seeks to create in his Petition, the issue raised on this appeal is not new or novel and is not one on which the Circuits are in conflict. Contrary to Waltman's characterization of the question presented on this appeal, the issue at hand is not whether the Federal Arbitration Act empowers arbitrators to award punitive damages or whether the Second Circuit's interpretation of that Act is at odds with that of the other Circuits. Rather, the decision under review is merely a decision by a federal court interpreting New York State substantive law on the availability of

punitive damages. Accordingly, the only conceivable question to review is whether the Second Circuit found and applied controlling New York law on this point.

Proceeding in federal court pursuant to diversity jurisdiction, the Southern District and Second Circuit correctly applied New York State law to determine whether or not this particular arbitration panel had the authority to award punitive damages. Contrary to Waltman's contention, the Circuits are not in conflict on the issue of whether state or federal substantive law applies in such a circumstance. Indeed, as the Second Circuit pointed out in the decision under review, this Court has already held that the propriety of an award of punitive damages in a diversity case is a question of state law. Browning-Ferris Indus. v. Kelco Disposal

Inc., 492 U.S. 257, 278 (1989).

Since it is undisputed that New York State law deprives arbitrators of the authority to award punitive damages, Garrity v. Lyle Stuart, Inc., 386 N.Y.S.2d 831 (1976), and there is no conflict among the Circuits as to the applicability of state law under these specific circumstances, there is no issue for this Court to decide which it has not already addressed.

Seeking to avoid the impact of Garrity, Waltman also argues that federal substantive law has so engulfed the field of arbitration as to preempt applicable state law. However, contrary to Waltman's contentions, this Court has also already held that the body of so-called federal substantive law does not totally preempt the entire field of arbitration. Volt Information Sciences v. Board of Trustees, 489 U.S. 468, 477

(1989). Since the preemption question has already been disposed of by this Court, there is no reason for the Court to reconsider that issue on these facts.

A. THIS COURT HAS ALREADY DETERMINED THAT FEDERAL SUBSTANTIVE LAW DOES NOT ENTIRELY PREEMPT THE FIELD OF ARBITRATION

While Waltman would have this Court find that the Federal Arbitration Act, 9 U.S.C. 1, et seq. ("FAA"), creates a body of federal substantive law which completely pre-empts state law with respect to the entire field of arbitration, this Court has already held in Volt, supra, that such is not the case. Waltman would also seem to have this Court find that simply because Fahnestock's underlying Petition to vacate the Award was brought in a federal court, a fortiori federal substantive law must govern the question of whether the arbitrators had the power

to render an award of punitive damages. That contention is similarly erroneous.

In Volt, this Court specifically held that the FAA does not create a body of federal substantive law which pre-empts the entire field of arbitration. Rather, state law will only be pre-empted "to the extent that it actually conflicts with federal law." Id. at 477. Stated differently, preemption is found only where state law stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress. Hines v. Davidowitz, 312 U.S. 52, 67 (1941).

As Judge Leisure stated in the Southern District opinion, New York State substantive law as set forth in Garrity regarding the inability of arbitrators to award punitive damages is not in direct or actual conflict with

any express provision of the FAA. At best, the purpose of the FAA was to require only that parties comply with their private agreements to arbitrate. Garrity does not stand as an obstacle to that purpose. The Second Circuit again made this clear as recently as three months ago in Barbier v. Shearson Lehman Hutton, Inc., 948 F.2d 117 (2d Cir. 1991). A party cannot be compelled to submit to arbitration any dispute which he has not agreed to so submit. AT&T Technologies v. Communications Workers of America, 475 U.S. 643, 648 (1986). Thus, contrary to the argument made by Waltman, this Court has already decided that the FAA does not entirely preempt this field and Volt does not mandate resort to federal substantive law to dispose of the instant issue.

B. WHERE FEDERAL JURISDICTION IS BASED ON DIVERSITY, THE PROPRIETY OF AN AWARD OF PUNITIVE DAMAGES IS CONTROLLED BY FORUM STATE LAW

Waltman's Petition also casually ignores the fact that the underlying arbitration was not brought pursuant to the Federal Arbitration Act. Rather, federal jurisdiction in this proceeding, brought after the fact as a vehicle to vacate the Award, was predicated on diversity of citizenship of the parties. The underlying arbitration was an NYSE arbitration, held in the State of New York and governed by the laws of that state. The underlying claims of both Fahnestock and Waltman were similarly subject only to New York law. Indeed, focusing for the moment only on Waltman's counterclaim for defamation, it could only be resolved as a matter of New York law since there is no federal substantive law of defamation.

Accordingly, it is axiomatic that pursuant to Erie v. Tompkins, 304 U.S. 64 (1938), a federal court considering this issue would have no choice but to apply the law of the forum state. Under such circumstances, federal law mandates that a federal court look to state law for determining the availability of damages, including the availability of punitive damages. See e.g., Browning-Ferris, supra; Matthews v. CTI Container Transport Inter Inc., 871 F.2d 270 (2d Cir. 1989); Juster v. Rothschild, Unterberg, Towbin, 554 F.Supp. 331 (S.D.N.Y. 1983); Leidesdorf v. Fireman's Fund Ins. Co., 470 F.Supp. 82 (S.D.N.Y. 1979).

Similarly, the measure of damages generally, in a diversity case, is a matter controlled by state substantive law. See, e.g., Shu-Tao Lin v.

McDonnell Douglas, 742 F.2d 45, 49 (2d Cir. 1984).

Here, arbitration was invoked pursuant to the Rules of the NYSE and the underlying dispute is one between a New York employer (Fahnestock) and its former employee, employed in its New York office (Waltman). Federal jurisdiction was never sought or acquired in connection with the commencement of the underlying arbitration or the enforceability of the NYSE rules requiring members and their employees to submit their disputes to arbitration. Both Fahnestock and Waltman could have proceeded in New York State court to enforce or vacate the Award.

The theory being advanced by Waltman would yield an anomalous and irrational result. If Waltman is arguing that federal substantive law applies to the

remedy imposed by the arbitrators in the instant case solely because the Petition to vacate was brought in federal, as opposed to state, court, such a holding would act to encourage and reward forum-shopping. Where parties have not contractually agreed to arbitrate the issue of punitive damages, parties to New York arbitral awards which include punitive damages would face different results depending upon whether confirmation was sought in New York state as opposed to federal courts. This would produce a race to the courthouse, as victorious parties would seek to confirm in federal court before the losing party could run to state court to get the award vacated. The same forum shopping would occur among Districts and Circuits. Such a result is neither the letter nor the intent of the law. The outcome should be the same

whether Fahnestock or Waltman sought to confirm or vacate in New York's state or federal courts or whether, by virtue of diversity, confirmation or vacatur was sought in some other District or Circuit. Any federal court, whose jurisdiction was invoked by virtue of diversity, should reach the same result. This Court has already made it clear that under such circumstances, the laws of the forum state must apply. The law of this forum state, New York, is clear. Arbitrators under these facts are not empowered to award punitive damages and the Second Circuit correctly found such state law to be controlling.

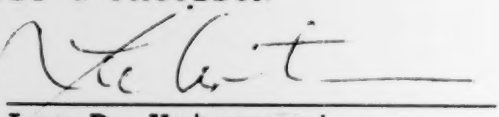
CONCLUSION

For the reasons set forth above, Waltman's Petition for a writ of

certiorari should be denied.

Respectfully submitted,

BROUDY & JACOBSON

By: 

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No. 91-699

In The

Supreme Court of the United States

October Term, 1991

JOSEPH J. WALTMAN,

Petitioner,

vs.

FAHNESTOCK & CO., INC.,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

REPLY BRIEF FOR PETITIONER

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PETITIONER'S REPLY MEMORANDUM

Fahnestock & Co., Inc., in a footnote in its opposing brief in No. 91-699, urges the Court to reconsider its denial of Fahnestock's prior Petition for a Writ of Certiorari, No. 91-508 and bases this extraordinary request on "the subsequent publication of a decision by New York's Appellate Division," implying that there has been some change in the law (Brief in Opposition, page 1). In so doing, Fahnestock has deliberately misled the Court. The New York decision in question, *Herzfeld & Stern v. Beck*, 572 N.Y.S. 2d 683 (1st Dept. 1991) was decided on August 1, 1991, more than one month before Fahnestock filed its Petition. Fahnestock's suggestion that the decision was rendered subsequent to its filing or to the Court's denial of the Petition is thus a total misrepresentation. Respondent also suggests that the *Herzfeld* case is now the law of the State of New York. In fact, on November 27, 1991, a motion for leave to appeal to the New York Court of Appeals was filed on behalf of Warren Beck and the Court of Appeals has not decided the matter. Therefore, the Appellate Division opinion does not represent the law of the highest court of the State of New York and is not binding on any federal court.

Fahnestock's egregious misrepresentation concerning its previously denied petition is but one of many factual misrepresentations in its Brief.

In light of Fahnestock's disregard for its obligations pursuant to Rule 11 of the Federal Rules of Civil Procedure, Waltman believes not only that Fahnestock's untimely and dishonest request for reconsideration should be denied but that sanctions should be imposed on Fahnestock for causing Waltman to incur unwarranted expense in order to correct this critical misrepresentation.

Respectfully submitted,

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